



Guest Contributor: Proxy Access Could Hurt the Bottom Line

GUEST CONTRIBUTOR POST: *Brian G. Cartwright is senior advisor to Latham & Watkins LLP and a fellow of the Arthur and Toni Rembe Rock Center for Corporate Governance at Stanford University. Charles M. Nathan is a member of the corporate department in Latham & Watkins' New York office, is co-chair of the firm's Corporate Governance Task Force and is former global co-chair of the firm's Mergers and Acquisitions Group. This post is exclusive to The Conference Board Governance Center.*

By **Brian G. Cartwright and Charles M. Nathan**

The SEC's adoption of proxy access on Aug. 25 is a watershed event of potentially historic significance, climaxing over four decades of activist effort aimed at the boardroom

The legendary community organizer Saul Alinsky invented what he dubbed the "proxy tactic" during his late-1960s-era agitations against Eastman Kodak in Rochester, N.Y. As Alinsky wrote in his famous 1971 guide *Rules for Radicals*, before then "[n]o one had ever organized a campaign to use proxies for social and political purposes." But as Alinsky thought about the idea, "[s]oon I was intoxicated by the possibilities. You could begin to play the whole Wall Street board up and down." While Alinsky realized that "corporations will fight back by pointing out that the ... demands of the stockholders will result in diminished dividends," he believed enough stockholders would find their campaigns "more important than a cut in dividends." Alinsky was so excited by his new idea, that he trumpeted the proxy tactic as "one of the single most important breakthroughs in the revolutions of our times."

Well, now we shall see whether Alinsky was right. At a moment when our economy is tottering, millions are unemployed with little hope of relief, and American economic dominance is challenged by aggressive new competitors in Asia, a bare party-line majority of the SEC has embarked on a grand experiment in politicizing the leadership of our businesses.

Where once public company directors served on what were, in effect, self-perpetuating boards of trustees, now they find themselves newly transformed into a specialized form of politician coping with an annual election cycle. Corporate governance activists are busily laying an additional foundation for the politicization of corporate boards by agitating for vastly increased shareholder ability to call special meetings between annual elections, at which directors could face removal votes if they have sufficiently displeased the governance activists. Directors who looked forward to continuing to add value at the end of their career using business skills honed over a lifetime now will find themselves, like Donald Trump's reality show apprentices, subject to firing in public.

At least some directors more attuned to working on increasing market share than working on turning out the "political base" may head for the exits, and boardroom headhunters eagerly look forward to a boom in business. Of course, most directors will continue to be re-elected most of the time – just like members of Congress, whose 90+ percent re-election rate fails to render their conduct any less political.

And what about the little guy—the individual investor? Unfortunately, the little guy could end up taking it on the chin—and not just because generally only the biggest institutional stockholders will be in a position to use the new rules.

Why? Because proxy access will work mostly in the shadows. Those who control voting decisions by big institutional stockholders are consumed by a corporate governance agenda that is often divorced from value creation for shareholders and populist in substance and tone. Moreover, many of these institutional investors are controlled by special interests—the labor unions and the politicians who run or appoint the managers of huge public employee pension plans.

The large institutional investors are insisting on face-to face meetings with directors so they can make their wishes known directly when "culturally acceptable" and, when not, by more subtle methods. They won't find it hard, for example, to signal that "we'd prefer you build plants in the U.S. even if more expensive than overseas" or "we'd prefer you didn't take that strike" or "we'd rather you invest in more expensive green energy."

Directors who don't want a proxy fight will quietly go along. In most cases, no one would ever have to know: the new SEC rules don't require disclosure of such conflicts and contacts.

But enough conversations and decisions like that and entrepreneurship and profits will take an unseen hit. Extrapolate that across the entire economy and, not only the individual investor, but American prosperity also could take an unseen hit, just when we're most vulnerable.

Dodd-Frank Act

- **Advisory vote on executive pay**
- **Proxy access for shareholders to nominate directors**
- **Disclosure of chair and CEO structure**
- **Standards for independent compensation consultants**
- **Clawback language for executive compensation**